Attorney Docket No.8102P001 Patent

IN THE UNITED STATES PATENT AND TRADEMARK OFFICE

In Re the Application of : Gordon P. Getty	Examiner: Pollock, Gregory A.
	Art Unit: 3695
Application No.: 10/092,005	Confirmation No: 7579
Filed: March 6, 2002	
For: SYSTEM AND METHOD FOR PROVIDING LIQUIDITY	

Commissioner for Patents
P.O. Box 1450
Alexandria, VA 22313-1450.

DECLARATION OF WAYNE H. WAGNER UNDER 37 C.F.R. §1.132

I, Wayne H. Wagner, hereby declare that:

1. I am a citizen of the United States, and am currently a resident of the city of Venice in the state of California.

2. I am presently self employed as a part-time consultant and have almost 50 years of experience in the financial services industry. I have a Master of Science degree in Statistics/Management Science from Stanford University (1961). I was asked to serve as an independent director of ReFlow, LLC on the basis of my

expertise in the measurement of the costs of trading securities, derived from my founding of Plexus Group, which specialized in assisting investment managers, pension sponsors, brokerage firms and securities exchanges in achieving better, lower cost execution of securities transactions. At the time Plexus Group was sold to JPMorgan in 2001, Plexus had 187 clients and was a consultant to 17 of the top 20 investment managers in the world. In November of 2009, ReFlow reorganized its board of directors and I ended my service as an independent director. I currently hold no financial interest in ReFlow. I shall be compensated by ReFlow, however, for my time spent in connection with the preparation of this Declaration.

3. Prior to forming Plexus Group, I was Chief Investment Officer at Wilshire Asset Management, managing over $2 billion dollar in pension assets. I am the author or co-author of almost 100 publications and I have given nearly 300 speeches during my career. I taught Trading and Markets as an Adjunct Professor at the Marshall School of Business at the University of Southern California and as a Visiting Professor at the Anderson School of Management at UCLA. I have authored four books, including The Complete Guide to Securities Transactions, John Wiley & Sons (1986) and Investment Management: Meeting the Noble Challenges of Funding Pensions, Deficits and Growth, John Wiley & Sons (2009).

4. Having worked in the financial services industry for nearly 50 years, I am familiar with the challenges involved both in managing mutual funds and in supplying services related to mutual funds, prior to and subsequent to ReFlow offering Redemption Service.

5. The ability for mutual fund investors to buy and sell securities daily is an important feature of mutual funds since it provides shareholders with liquidity upon demand. However, large payouts to shareholders can penalize investment performance by triggering expensive securities transactions by selling fund holdings. For example, if a fund experiences $10 million in net redemptions but holds only $1 million in cash, the manager may be forced to either sell mutual fund holdings or secure a loan. (Discussed in paragraphs 10 and 11 below.) In response to these needs, ReFlow provides a unique, pioneering service to mutual funds that helps fund managers improve performance by reducing transaction costs attributable to investor generated cash outflows.

6. The effects of cash flows on investment performance have in previous decades been largely ignored in the belief that superior stock selection would dominate any cost considerations. This optimistic attitude was severely bruised in the 1970's by academic developments in the areas of performance measurement, risk adjustment, and cost-efficient index funds. Nonetheless, little attention was paid to the costs mutual funds sustain from shareholder-generated cash flows until the end of the boom markets of the 1990's subjected funds to significant and continuing redemptions. In recent decades, investors have retained a new breed

of asset allocators to provide recommendations for the timing of funds and sectors. The asset redistributions produced by these allocators have significantly increased the magnitude and frequency of mutual fund flows. Finally, the studies of Roger Edelen (see paragraphs 10 and 11) provide academic evidence of how net share redemptions trigger difficult and costly trading.

7. ReFlow's innovative method uses an Internet-based system that allows mutual fund managers to minimize the disturbance effects of shareholder liquidity demands, allowing the managers to focus on enhancing portfolio returns rather than reallocating assets to match fund flows. As a result, more fund assets remain invested while cash reserves, transaction costs and taxable events are reduced, resulting in more efficient portfolio management.

8. Since its founding in 2002, ReFlow has offered the Redemption Service, which includes the features set forth in the independent claims of the above-referenced patent application. In particular, Redemption Service is offered to investment funds wanting to receive liquidity services to facilitate the fund's meeting of financial obligations resulting from a net share outflow – i.e., an excess number of shares being redeemed, excluding shares redeemed by ReFlow, in comparison to a number of shares being purchased, excluding shares purchased by the ReFlow, over a predetermined amount of time – e.g., on a daily basis.

9. An investment fund registers with ReFlow's Redemption Service and is prompted to offer shares to ReFlow in response to the determination that the registered

investment fund has a net share outflow/redemptions. ReFlow purchases one or more of the offered shares from the mutual fund (e.g., at the daily strike price), holds them for a period of time (e.g., up to 28 days), and redeems them in response to any net inflows generated by fund shareholders. Any shares held by ReFlow not redeemed within 28 days must be redeemed at the end of the period. This final redemption can be anticipated well in advance, reducing the problems of expensive forced trades.

10. For the past 20 years, liquidity has become increasingly important to mutual funds as investors have been shifting assets at an ever-increasing pace. One long unsolved problem intensified by asset shifting is that fund managers must provide cash on demand to cover net share redemptions. As a result, managers have relied on the following three methods to meet liquidity needs in response to net share redemptions:

    a. Holding a large cash buffer within the mutual fund to cover anticipated redemptions. Holding cash has helped fund managers respond to net share redemptions, but many managers want to be as fully invested as possible to maximize the shareholders' return on investment. Maintaining a significant average cash potential to cover net redemptions causes a drag on performance.[1] For example, funds often hold more cash during

---

[1] Exhibit A: "A Survey of the Evidence on the Cost of Mutual Fund Flows," Roger M. Edelen, Assistant Professor of Finance, The Wharton School, University of Pennsylvania, ReFlow website archived Nov. 26, 2002 by Internet Archive (http://web.archive.org/web/20021126134525/http://www.reflow.com/ accessed on 10/29/2010).

market upswings than in downswings, resulting in missed opportunities for return on investment.[2]

b. Selling some of the security holdings of the mutual funds. These transactions come with significant cost: commissions, excessive price impact triggered by forced selling, taxable events to the shareholders, time spent managing the fund to address liquidity, etc. Importantly, the timing of those redemptions can be highly disadvantageous if shareholders are prompted to sell by sharp market declines. In an attempt to reduce the costs and performance effects of net share redemption driven trades, fund managers turned to new trading tools, including transaction cost analysis, alternative trading venues, and trading via futures and exchange-traded funds. These efforts were incomplete, however, because while they reduce the costs of selling the underlying assets, they do not eliminate the need to sell the underlying assets.

c. Relying upon loans or lines of credit to provide short term liquidity. These arrangements, usually arranged through broker/dealers, can be difficult to secure and are often expensive to establish and maintain.[3]

---

[2] Exhibit B: "Marketing the Benefits of ReFlow to Investors" Roger M. Edelen, Assistant Professor of Finance, The Wharton School, University of Pennsylvania, ReFlow website archived Nov. 26, 2002 by Internet Archive (http://web.archive.org/web/20030424231236/www.reflow.com/reflow_marketing_prn.htm accessed on 10/29/2010).

[3] Exhibit C: "American independence Funds Adopt ReFlow Liquidity Service," ReFlow Press Release dated November 19, 2008 (http://www.reflow.com/releases/PR2008-11-19.htm accessed on 10/29/10).

11. ReFlow's Redemption Service, as presently claimed in the above-referenced patent application (with reference to the claims of the Amendment enclosed herewith), allows mutual fund managers to cover the net share redemption without disturbing assets, drawing on cash reserves, or relying on expensive loans or lines of credit. When net share redemptions exceed the determined amount, the fund can offer shares to ReFlow. Reflow's Redemption Service is less expensive than borrowing against a loan or line of credit or maintaining an excessive cash reserve. As a result, costs and taxable events are reduced and the fund may experience improved performance for fund shareholders.

12. The following hypothetical situation is provided to explain the process. A hypothetical manager of a foreign bond portfolio over breakfast sees in the news that the Euro has plunged overnight. He knows there are some "hot money" investors in his fund, and they will react to this news by tendering shares for redemption. More seriously, he knows that the market today for his thinly traded bonds will be very illiquid. At times past, he had to trade in those panicked markets to raise cash for the redemptions, taking whatever price he could obtain on any bond for which he could find a buyer. His broker would lend some money, but with the markets in turmoil, overnight LIBOR funds would be very expensive. If his fund directors signed up with ReFlow's Redemption Service, and he can offset those redeemed shares when ReFlow buys them, offsetting the cash flow and avoiding all the negative impact on fund costs and holdings diversification. Later, when things calm down, he can repurchase the ReFlow

shares with money coming in to his fund, or liquidate the ReFlow shares in an orderly manner over the next four weeks.

13. ReFlow's unique and innovative Redemption Service was not instantly accepted as the preferred solution to liquidity problems resulting from a net share redemption. After years of persistent efforts, however, the features of Redemption Service set forth in the claims of the present application have found commercial success. To date, ReFlow's Redemption Service has been approved by the Boards of Directors of 26 mutual fund families, primarily in the United States but also in Europe: for some years ReFlow operated an office in Luxembourg, a financial center for European mutual funds. ReFlow's client base represents more than $440 billion in assets, distributed across 460 funds. ReFlow has provided more than $3.3 billion in capital in over 3300 transactions.

14. It is difficult to determine Redemption Services' percentage of the market share of liquidity services for mutual funds in general since the competition for liquidity services is only via the more traditional forms of excess cash holdings, sales of mutual fund holdings to meet liquidity demands, and/or loans/lines of credit. ReFlow's Redemption Service is unique and, therefore, accounts for 100% of the market share of this particular type of liquidity services. Additionally, the continuing use of Redemption Services by client mutual funds indicates that real value is being supplied.

15. The level of scrutiny required from a mutual fund's Board of Directors to authorize ReFlow's Redemption Service indicates that Redemption Service's continuing success and client retention is attributed to the merits of the features claimed in the present application and is not merely the result of heavy promotion or advertising, shift in advertising, consumption by purchasers normally tied to applicant or assignee, or other business events extraneous to the merits of the claimed invention.

16. In addition, in accordance with the No-Action Letter from the SEC, the Board of Directors of a participating mutual fund must find that the fund's participation is in the best interest of the fund and its shareholders.[4] Furthermore, this finding is provided solely to ReFlow and the participating mutual fund and "may not be relied upon by any other party."[5]

17. The above statement also suggests a reason why ReFlow has no direct competitors. One attempt to mimic the ReFlow services was made by a firm called Ebb Services ("Ebb"). This attempt was unsuccessful, and the firm dissolved before attracting any clients or completing any transactions. Although Ebb tried to position itself as an alternative to ReFlow, the model put forth was

[4] Exhibit D: No-Action Letter under: Investment Company Act of 1940- Section 18(f), 22(d); Rule 12b-1, 22c-1, U.S. Securities and Exchange Commission, July 15, 2002 (http://www.sec.gov/divisions/investment/noaction/reflow071502.htm accessed on 10/29/2010).

[5] Id.

very different from the ReFlow offering in the following ways.

a. Ebb had no clearance from the Securities and Exchange Commission.
b. Ebb required participating fund families to make a portfolio investment in Ebb, which for some funds could have represented the largest holding (in an unknown and untried concept!)
c. Ebb's portfolio, purportedly designed to track the mutual funds, was run by a black box application called ELF. The ability of ELF to simulate actual fund performance was unproven.
d. Ebb's service was not successful and Ebb closed its doors.

18. Prior to enjoying the commercial success described above, ReFlow's Redemption Service was met with initial incredulity and skepticism. ReFlow's Redemption Service was viewed as "ivory towered," doubts were expressed as to whether such an approach could be favorable to either the mutual funds or ReFlow, and, instead, "[c]onventional bank financing would seem to be the method of choice."[6] The named inventor of the above-referenced patent application, Gordon Getty, in an interview in 2004 (approximately one year after the initial offering of Redemption Service) admitted that Reflow's Redemption Service did not have an easy start and that it would take time to make a profit because "[t]his is an off-the-wall idea … out-of-the-box. It just is going to take time for people to bite. … It is such an unusual concept, a natural reaction of fund

[6] Exhibit E: "Getty to play rich uncle for a price," Investment News, August 26, 2010 (http://www.investmentnews.com/article/20020826/SUB/208260703 accessed on 10/29/2010).

boards would be, 'If this thing works, how come it wasn't thought of 50 years ago?'"[7] In the initial years of operation, ReFlow's only clients were affiliated companies of the Forward Funds group, of which Getty was the majority shareholder. After completing nearly 600 transactions with Forward Funds, however, ReFlow had ample data for prospective clients to view and was ready to prove that the skeptics were wrong.[8] As set forth in paragraphs 13-15 above, ReFlow's Redemption Service subsequently overcame the initial skepticism it faced and found commercial success.

19. I have reviewed U.S. Patent No. 7,035,820 by Goodwin et al. ("Goodwin"), U.S. Patent Publication No. 2003/0074300 by Norris ("Norris"), and U.S. Patent No. 7,249,075 by Altomare ("Altomare"). I have also reviewed the present application and what I understand to be the currently pending claims (as set forth in the Amendment enclosed herewith). I consider ReFlow's Redemption Service to be an embodiment of the invention described and claimed in the present application. In addition, I consider the invention as described in the claims to be novel and non-obvious. ReFlow's Redemption Service has been repeatedly recognized as a novel technique for improving mutual fund performance.[9] Goodwin, Norris, and Altomare, alone or in combination, do not disclose determining that a registered

[7] Exhibit F: "Getty says his 'off-the-wall' fund idea will work," Reuters, March 17, 2004.

[8] Exhibit G: "Getty's ReFlow, at take-off point, to seek funding," Reuters, June 22, 2005.

[9] *see* Exhibits G and H: "Getty's ReFlow, at take-off point, to seek funding," Reuters, June 22, 2005 and "Redemptions Force More Funds to Liquidate," SmartMoney, November 12, 2008, (http://www.smartmoney.com/investing/mutual-funds/Redemptions-Force-More-Funds-to-Liquidate accessed on 10-29-10).

investment fund has a net share outflow. For example, the Examiner alleges that Altomare discloses this feature as it is currently claimed. Altomare describes managing a trust with a particular ratio of U.S. Treasury STRIPS and shares of stock. The combination of STRIPS and stock is characterized in units of the trust which can be bought and sold. Periodic distributions are calculated based upon comparisons of current value of the trust units to a pre-set par value and excess value payments may be reinvested. Altomare, however, is silent regarding an investment fund having a net share outflow as claimed in the present application. Without said determination, none of Goodwin, Norris, and Altomare is able to prompt an investment fund to offer shares ***in response to the determination that investment fund has a net share ouflow***. The general concept of buyer/seller alerts described by Goodwin is not equivalent to prompting, in response to the determination that the registered investment fund has net share redemptions, the registered investment fund to offer shares to the liquidity vehicle. Furthermore, none of the references describe a net inflow of shares. As a result, the combination of Goodwin, Norris, and Altomare also fails to disclose redeeming at least one purchased share from the registered investment fund ***in response to a net inflow of shares*** of the registered investment fund. The combination of references only teaches, via Goodwin, the termination of a repurchase agreement based upon a fixed timeline – <u>not</u> the redemption of a share in response to a net inflow of shares of the registered investment fund.

I hereby declare that all statements made herein of my own knowledge are true and that all statements made on information and belief are believed to be true; and further that these statements were made with the knowledge that willful false statements and the like are punishable by fine or imprisonment, or both, under Section 1001 of Title 18 of the United States Code, and that such willful false statements may jeopardize the validity of the above-identified application or any patent issued thereon.

Executed on December 27, 2010 at San Francisco California.

By: Wayne H. Wagner

Wayne H. Wagner
2201 Ocean Front Walk
Venice, CA 90291